



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

Report of the auditor-general to the North West provincial legislature and the council on the Naledi Local Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of the Naledi Local Municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2014 (Act No. 10 of 2014) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.



Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Naledi Local Municipality as at 30 June 2015 and its financial performance and cash flows for the year then ended, in accordance with SA standards of GRAP and the requirements of the MFMA and the DoRA.

Emphasis of matters

7. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

8. As disclosed in note 34 to the financial statements, the corresponding figures for the year ending 30 June 2014 have been restated as a result of errors discovered during the year ending 30 June 2015 in the financial statements of the Naledi Local Municipality at, and for the year ended, 30 June 2014.

Unauthorised, irregular and fruitless and wasteful expenditure

9. As disclosed in note 35.1 to the financial statements, unauthorised expenditure of R52 783 162 was incurred in the current year and the unauthorised expenditure in respect of prior years of R54 322 626 had not yet been dealt with in accordance with section 32 of the MFMA.
10. As disclosed in note 35.2 to the financial statements, fruitless and wasteful expenditure of R17 671 394 was incurred in the current year and fruitless and wasteful expenditure from prior years of R14 645 586 had not yet been dealt with in accordance with section 32 of the MFMA.
11. As disclosed in note 35.3 to the financial statements, irregular expenditure of R2 440 875 was incurred in the current year and irregular expenditure from prior years of R151 294 378 had not yet been dealt with in accordance with section 32 of the MFMA.

Material impairments and losses

12. As disclosed in note 23 to the financial statements, impairments of R30 068 238 (2014: R40 924 920) were incurred as a result of significant impairment of debtors.
13. As disclosed in note 27 to the financial statements, material distribution losses of R11 218 757 (2014: R14 675 308) and R6 455 566 (2014: R5 091 482) were incurred as a result of electricity and water losses respectively.

Going concern

14. As disclosed in note 45 to the financial statements the Naledi Local Municipality incurred a net loss of R323 728 140 during the year ended 30 June 2015 and, as of that date, the Municipality's current liabilities exceeded its current assets by R315 236 919. These conditions, along with other matters as set forth in note 45, indicate the existence of a material uncertainty that may cast significant doubt on the Municipality's ability to operate as a going concern.

Significant uncertainties

15. With reference to note 40 to the financial statements, the municipality is the defendant in a number of legal matters. The municipality is contesting these claims. The ultimate outcome of the matter cannot presently be determined and no provision for any liability that may result has



been made in the financial statements.

Additional matters

16. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited disclosure notes

17. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

Unaudited supplementary schedules

18. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

Report on other legal and regulatory requirements

19. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for selected development objectives presented in the annual performance report, compliance with legislation and internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

20. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development objectives presented in the annual performance report of the Municipality for the year ended 30 June 2015:

- Development objective: To promote uninterrupted basic service delivery on pages x to x
- Development objective: To report on national general KPIs on pages x to x

21. I evaluated the reported performance information against the overall criteria of usefulness and reliability.

22. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development objectives. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's Framework for managing programme performance information (FMPPI).

23. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

24. The material findings in respect of the selected development objectives are as follows:

Development objective: To promote uninterrupted basic service delivery



Usefulness of reported performance information

25. The FMPPPI requires that indicators be well defined and verifiable and targets be specific, measureable and time bound:

- A total of 67% of the targets were not specific.
- The required performance for 67% of the targets could not be measured.
- A total of 67% of the indicators were not well defined.
- A total of 33% of the indicators were not verifiable.

This was because management was not aware of the requirements of the FMPPPI.

26. The FMPPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. A total of 67% of the indicators did not relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives as per the integrated development plan (IDP) and the service delivery and budget implementation plan (SDBIP). This was because proper performance planning and management practices had not been developed and implemented to provide for the development of performance indicators and targets included in the IDP and the SDBIP.

Reliability of reported performance information

27. The FMPPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to limitations placed on the scope of my work due to the absence of information systems and the auditee's records not permitting the application of alternative audit procedures.

Development objective: To report on national general KPIs

Usefulness of reported performance information

28. The FMPPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. A total of 45% of the indicators did not relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives as per the IDP and the SDBIP. This was because proper performance planning and management practices had not been developed and implemented to provide for the development of performance indicators and targets included in the IDP and the SDBIP.

Reliability of reported performance information

29. The FMPPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to limitations placed on the scope of my work due to the absence of information systems and the auditee's records not permitting the application of alternative audit procedures.

Additional matters

30. I draw attention to the following matters:



Achievement of planned targets

31. Refer to the annual performance report on pages XX to XX and XX to XX for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected development objectives reported in paragraphs XX to XX of this report.

Adjustment of material misstatements

32. I identified material misstatements in the annual performance report submitted for auditing on the reported performance information for the Development priority: To report on national general KPIs. As management subsequently corrected only some of the misstatements, I identified material findings on the usefulness and reliability of the reported performance information.

Unaudited supplementary schedules

33. The supplementary information set out on pages XX to XX does not form part of the annual performance report and is presented as additional information. I have not audited this schedule and, accordingly, I do not report thereon.

Compliance with legislation

34. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Strategic planning and performance management

35. The performance management system and related controls were inadequate as it did not describe and represent the processes of performance planning and improvement and how it is conducted, organised and managed as required by section 38 of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and regulation 7 of the Municipal planning and performance management regulations (MPPMR).
36. Measurable performance targets for the financial year were not set in the IDP, for each of the key performance indicators and with regard to each of the development priorities or objectives, as required by section 41(1)(b) of the MSA and the Municipal planning and performance management regulations 12(1) and 12(2)(e).

Annual financial statements

37. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, current assets, non-current liabilities, current liabilities and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, resulting in the financial statements receiving an unqualified audit opinion.

Expenditure management

38. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.



39. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Procurement and contract management

40. Bids were not always evaluated by bid evaluation committees which were composed of officials from the municipality's requiring the goods or services as required by SCM regulation 28(2).
41. Thresholds for local content on designated sectors procurement were not properly applied in accordance with the requirements of regulation 9 of the Preferential Procurement Regulations.
42. Awards were made to providers who are in the service of other state institutions in contravention of section 112(j) of the MFMA and SCM regulation 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).
43. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e).

Consequence management

44. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.
45. Allegations of financial misconduct laid against officials of the municipality were not investigated in accordance with the requirements of sections 171(4)(a) and 172(3)(a) of the MFMA and regulation 5(1) of the Municipal regulations on financial misconduct procedures and criminal proceedings.

Audit committee

46. The performance audit committee did not make recommendations to the council, as required by regulation 14(4)(a)(ii) of the MPPMR.

Budget

47. The total unforeseen and unavoidable expenditure incurred exceeded the greater of R5 million or 4% of own revenue, in contravention of regulation 72 of the Municipal Budget and Reporting Regulations.

Environmental matters

48. The municipality did not exercise its legislative and executive authority as required by the sections 11(3)(l) and (m) of the MSA by managing, monitoring and enforcing environmental related bylaws to promote a safe and healthy environment.
49. The municipality operated one of its waste disposal site facilities without a license in contravention of section 20(b) of the National Environmental Management Waste Act, 2008 (Act No. 59 of 2008) (NEMWA), section 24(2)(a) of the National Environmental Management Act, 1998 (Act No. 107 of 1998) (NEMA) and section 22(1)(b) of the National Water Act, 1998 (Act No. 36 of 1998) (NWA).
50. The municipality's waste management and disposal activities contravened the requirements of section 28(1) of the NEMA, section 19 of the NWA and sections 16(1)(c) and (d) and 26(1)(b) of the NEMWA.



Internal control

51. I considered internal control relevant to my audit of the financial statements, the annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

52. The leadership did not exercise adequate oversight over financial and performance reporting, compliance monitoring and related internal controls. Policies and procedures did not adequately guide financial, performance and compliance activities.

Financial and performance management

53. Management's internal controls and processes over the preparation and presentation of financial statements and performance reports were not able to ensure that the reports were free from material misstatements. As a result, material corrections had to be made to the audited annual financial statements and performance reports.

Governance

54. The internal audit department did not have an impact as their recommendations were not always implemented during the financial year. Although the audit committee fulfilled its functions during the year, they had limited impact due to the lack of adequate implementation of their recommendations by the municipality.

Auditor General

Auditor-General

Rustenburg

30 November 2015



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